

POWER TIP

There Are Losses and There Are Losses

As the Oracle himself, Warren Buffett, has said many times when it comes to investing: *Rule #1: Don't lose money. Rule #2: Don't forget Rule #1.* But many people misinterpret this message and pay the long-term price of inferior investment returns for the error. Buffett is specifically *not* saying don't lose money *ever*. On the contrary, he is also quoted as saying you should be prepared to lose as much as 50% on a given stock post-purchase. How do you reconcile these seemingly contradictory concepts?

The answer is subtle and simple, but powerful.

When Buffett says don't lose money, he is referring to *permanent capital losses*. He is saying, in effect, do not make stupid investments in the stocks of low-quality companies that you know nothing about and that might see their price go to zero...permanently. But having the stock of a quality company go down 30%, 40%, 50% due to uncontrollable market forces before heading back north to the land of profits? No problem. (After buying GE in 2008, Buffett experienced near-term losses of more than 50% in a matter of weeks.) Expect it, welcome it, for you can then buy more stock at a lower price, a common practice of the superior investor.